

Media Release:

China Steel Structure Co. Ltd. Outlook Revised To Stable From Negative On Similar Parent Action; 'twA-/twA-2' Ratings Affirmed

April 23, 2021

Rating Action Overview

- Taiwan-based China Steel Structure Co. Ltd. is the first local company to specialize in steel structure production. It had EBITDA of NT\$530 million in 2020.
- We recently revised up the outlook on China Steel Structure's parent company, China Steel, to stable from negative.
- On April 23, 2021, we revised our outlook on the long-term issuer credit rating on China Steel Structure to stable from negative. At the same time, we affirmed our 'twA-' long-term and 'twA-2' short-term issuer credit ratings on China Steel Structure.
- The stable outlook reflects the outlook on the parent, China Steel, and indicates our expectation of a recovery in the parent company's credit metrics in 2021. In addition, the stable outlook reflects our view that China Steel Structure will remain a strategically important subsidiary to the China Steel group over the next two years.

Rationale Action Rationale

The outlook on China Steel Structure follows that on its parent company. The outlook revision on **China Steel Structure Co. Ltd.** follows similar action we took on the outlook on the long-term rating on its parent company, **China Steel Corp.** This reflected the strong recovery in the global steel industry which could improve China Steel's operating performance over the next 12-24 months. We believe China Steel's ratio of funds from operations (FFO) to debt could grow to 25%-28% in 2021 from 13% in 2020, due to recovering sales and profit margin with declining debt guarantees. However, steel output could ramp up globally in 2022 with intensifying competition, bringing downward pressure on steel prices and China Steel's profit margin, and potentially reducing China Steel's ratio of FFO to debt to 20%-23% in 2022.

The ratings on China Steel Structure reflect our view of the company's strategically important membership of the China Steel group. We assess China Steel Structure to be of strategic importance to the parent China Steel group by helping to maintain the group's position in the domestic steel market. The ratings on China Steel Structure also reflect the company's leading position in Taiwan's steel structure market and the company's strong interest coverage.

PRIMARY CREDIT ANALYST

Irene Lai
Taipei
+886-2-2175-6825
irene.lai
@spglobal.com
irene.lai
@taiwanratings.com.tw

SECONDARY CONTACT

Jin Dong, CFA
Taipei
+886-2-2175-6821
jin.dong
@spglobal.com
jin.dong
@taiwanratings.com.tw

Outlook

The stable outlook on China Steel Structure reflects the stable rating outlook on its parent, China Steel, and our expectation that China Steel Structure will remain a strategically important subsidiary to the group over the next two years. The stable outlook also reflects our expectation of a recovery in China Steel's ratio of FFO to debt in 2021, spurred by solid demand recovery, strong operating cash flow generation, and declining guarantee debts. However, this improvement could slow down as steel output restores in 2022 and somewhat weaken the steel price, China Steel's profit margin, and the company's ratio of FFO to debt.

Downward scenario

We could lower the long-term rating on China Steel Structure if:

- China Steel's ratio of FFO to debt weakens to close to 12% for an extended period, possibly due to (a) a prolonged COVID-19 outbreak that seriously damages the global economy and curbs economic recovery leading to an extensive industry downturn with contraction in demand and intense competition, (b) persistently high raw material prices which would squeeze the company's profit margin materially, or (c) China Steel adopts a much more aggressive capital expenditure (capex) plan that curbs its ability to deleverage and results in an elevated debt level for an extended period;
- We believe China Steel Structure's relationship with the parent group and potential group support weakens, as indicated by a decline in China Steel's ownership in the company;
- China Steel Structure's EBITDA interest coverage worsens to below 3x for an extended period which may result from a deteriorating operating margin caused by stiffer competition; or

Upward scenario

We may raise the long-term rating on China Steel Structure if we raise our assessment of the China Steel group credit profile and at the same time raise our assessment of China Steel Structure's standalone credit profile (SACP). We could raise the group credit profile if the group improves its profitability and lowers its debt, such that its ratio of FFO to debt rises to materially above 25% on a sustainable basis.

We could raise China Steel Structure's SACP if the company improves its ratio of liquidity sources to uses materially to close to 1.2x over the next 12 months, while at the same time maintain its EBITDA margin above 4%. This could happen if the company extends its debt maturity substantially while improving its market position and pricing power.

Ratings Score Snapshot

Issuer Credit Rating: twA-/Stable/twA-2

Note: The descriptors below are on a global scale.

Business Risk: Fair

- **Country risk:** Intermediate
- **Industry risk:** Moderately high
- **Competitive position:** Fair

Financial Risk: Aggressive

- **Cash flow/Leverage:** Aggressive

Anchor: twbbb

Modifiers

- **Diversification/Portfolio effect:** Neutral (no impact)
- **Capital structure:** Negative (-1 notch)
- **Financial policy:** Neutral (no impact)
- **Liquidity:** Less than adequate (no impact)
- **Management and governance:** Fair (no impact)
- **Comparable rating analysis:** Neutral (no impact)

Stand-alone credit profile: twbbb-

- **Group stand-alone credit profile:** twa+
- **Entity status within group:** Strategically important (+3 notches from SACP)

Related Criteria & Research

Related Criteria

- General Criteria: Principles Of Credit Ratings - February 16, 2011
- General Criteria: Group Rating Methodology - July 01, 2019
- General Criteria: Methodology: Management And Governance Credit Factors For Corporate Entities - November 13, 2012
- Criteria | Corporates | General: Corporate Methodology: Ratios And Adjustments - April 01, 2019
- Criteria | Corporates | General: Methodology And Assumptions: Liquidity Descriptors For Global Corporate Issuers - December 16, 2014
- General Criteria: Country Risk Assessment Methodology And Assumptions - November 19, 2013
- General Criteria: Methodology: Industry Risk - November 19, 2013
- Criteria | Corporates | General: Corporate Methodology - November 19, 2013

Related Research

- Media Release: China Steel Corp. Outlook Revised To Stable From Negative On Solid Demand Recovery; 'twAA-/twA-1+' Ratings Affirmed, April 23, 2021
- Taiwan Ratings' Ratings Definitions – August 10, 2020

(Unless otherwise stated, these articles are published on www.taiwanratings.com)

Ratings List

Ratings Affirmed; Outlook Revised

	To	From
China Steel Structure Co. Ltd.		
Issuer Credit Rating	twA-/Stable/twA-2	twA-/Negative/twA-2

Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at www.taiwanratings.com for further information. Complete ratings information is available to subscribers of Rating Research Service at rrs.taiwanratings.com.tw. All ratings affected by this rating action can be found on Taiwan Ratings' public website at www.taiwanratings.com.

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